

**DEPARTMENT OF VETERANS SERVICES  
AND  
THE VETERANS SERVICES FOUNDATION**

**REPORT ON AUDIT  
FOR THE PERIOD  
APRIL 1, 2006 THROUGH JUNE 30, 2007**



## **AUDIT SUMMARY**

Our audit of the Department of Veterans Services and the Veterans Services Foundation for the period April 1, 2006 through June 30, 2007, found:

- amounts reported in the Commonwealth Accounting and Reporting System accounting records were fairly stated, in all material respects;
- certain matters involving internal control and its operation that require management's attention and corrective action;
- instances of noncompliance that are required to be reported under Government Auditing Standards; and
- inadequate corrective action of prior year audit findings.

Management is responsible for strategic planning and ensuring that the agency's operations helps Veterans Services meet its goals. In order to efficiently and effectively operate an organization, management must establish an operating plan that describes how the organization will achieve its goals. We have concerns that management has not fully evaluated their environment and created this plan.

Last year, we recommended that Veterans Services evaluate their financial management issues and establish a proper oversight structure. We found that the agency has resolved some of the concerns we noted in the prior year's audit by establishing more review processes; however, management has not addressed all of the concerns, met its own internally-set corrective action plan, or established a proper oversight structure.

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## **STATUS OF PRIOR YEAR AUDIT FINDINGS**

Our prior report included various findings related to improving accounting and internal controls. As part of this review, we followed up on the status of these findings and summarized the progress below.

<b>Prior Year Finding</b>	<b>Status of Finding</b>
Establish Process for Determining Negotiated Rates	Resolved
Strengthen Controls over the Small Purchase Charge Card Program	Progress Made
Properly Report Construction in Progress	Progress Made
Implement and Monitor Procedures To Ensure Proper Use of Funds	Progress Made
Establish and Implement Adequate Policies and Procedures over the Veterans Services Foundation	Progress Made
Improve Voucher Documentation and Compliance with Procurement and Payment Policies	Progress Made
Establish a Memorandum of Understanding with the Department of General Services	Limited Progress Made
Ensure Accurate Time and Leave Reporting	Limited Progress Made
Improve Petty Cash Controls	Limited Progress Made
Appropriate Allocate Administrative Costs	Limited Progress Made
Information Systems Security Assurance	Limited Progress Made
Improve Petty Cash Records and Compliance with Requirements	Limited Progress Made
Comply with Commonwealth Human Resources Overtime Standards	Limited Progress Made
Improve Debt Collection Efforts and Account Write-offs	Limited Progress Made
Properly Manage Fixed Assets	Limited Progress Made

## **AGENCY ORGANIZATIONAL STRUCTURE AND FOCUS**

### *Background*

Before the formation of the Department of Veterans Services, the Department of Veterans' Affairs and the Veterans Care Center Board of Trustees were the two primary agencies serving Virginia's veterans. The Department of Veterans' Affairs assisted veterans and their families with applying for benefits and operated the Virginia Veterans Cemetery in Amelia. The Virginia Veterans Care Center Board of Trustees, a separate state agency, managed, controlled, maintained, and operated the Virginia Veterans Care Center, a long-term care facility. The Board of Trustees contracted with various private companies to operate the center. Additionally, the Department of Education reviewed, approved, and monitored post-secondary education and training programs for veterans under the State Approving Agency for Veterans Education program.

In 2002, the Governor created the Governor's Advisory Commission for Veterans' Affairs to review agencies and programs currently serving veterans, assess the current and future projected needs of Virginia's veterans, identify current and potential future funding sources, and recommend a structure for the most effective delivery of services to Virginia's veterans. The Advisory Commission determined that the responsibility, authority, and accountability for providing veteran services were scattered across multiple agencies, programs, and boards in the Administration Secretariat.

The Commission believed that the Commonwealth's arrangement of veterans programs had evolved over time in a haphazard manner. This development led to unclear priorities and an inconsistent methodology

to determine veterans' needs. As a result, there was an inefficient structure with administrative overlap and a lack of a clear and comprehensive mission for veterans services in the Commonwealth.

Based on their findings, the Commission suggested the restructuring of the agencies, programs, and boards into a single agency with a single policy board. This single agency could establish unity of command and mission that included converting the Virginia Veterans Care Center into a state-run operation. The Commission also recommended changes in the board structure by establishing one overall veterans' services policy board with specified responsibilities to address benefits, care centers, and cemeteries. In addition, the Commission suggested developing a concrete business plan for current and future operations of the Care Center. The Commission also suggested considering the need for more cemeteries and adopting a concrete business plan for the cemeteries.

Based on the Commission's report, the General Assembly passed legislation that followed the recommendations of the Commission to re-engineer existing veterans' service programs and consolidate them into a single agency. As a result of this legislation on July 1, 2003, the Department of Veterans Services (Veterans Services) came into existence to provide a "one-stop" service agency for veterans and their families. Veterans Services has an administrative division and four main service divisions: Benefits, Cemeteries, Care Center, and Veterans' education.

The legislation replaced the Department of Veterans' Affairs, the Virginia Veterans Care Center Board of Trustees, and the Virginia Veterans Cemetery Board and created three citizen boards, the Board of Veterans Services, the Joint Leadership Council of Veterans Service Organizations, and the Veterans Services Foundation. The Board of Veterans Services reviews the Commonwealth's existing veterans' services and recommends changes and improvements. The Joint Leadership Council of Veterans Service Organizations provides a vehicle for veterans' service organizations to collaborate with the Veterans Services in order to meet the needs of Virginia's veterans. The Veterans Services Foundation is responsible for raising funds, identifying existing revenue sources for veterans programs, and administering the Veterans Services Fund.

Since its formation, Veterans Services has added a second cemetery in Suffolk and a number of new veterans benefit offices. In late 2007, Veterans Services plans on opening a second long-term veteran's care center, Sitter-Barfoot Veterans Care Center (Sitter-Barfoot) in Richmond. This new center will cause a dramatic increase in the size and budget of the agency. Expansion plans also include a third veteran's cemetery in southwest Virginia and another veteran's care center in the Hampton Roads area.

### *Strategic Plan*

An organization's strategic plan sets the agency's mission, priorities, goals, and objectives. This plan describes the purpose for the organization's existence. In order to achieve its strategic plan, an organization should establish a functional operating plan. An appropriate operating plan will direct management and employees by setting-up the organization's structure and describe how processes will occur under this structure. This plan should describe the most efficient and effective way for the agency to operate, as well as allow management and employees to implement daily operating processes. Operating plans must also be sufficiently detailed to describe how each individual business unit should operate.

Veterans Services has as its mission serving Virginia's veterans and their beneficiaries by ensuring they receive the benefits, support, quality care, and recognition they have earned through service and sacrifice. However, we have concerns that management has not completely thought through how the agency will achieve this mission and its supporting goals.

Specifically, we believe that management has not considered the best way to operate multiple business units and the administrative section. A plan should exist which includes how each business unit and the administrative section will support the overall strategic plan. This plan will ensure that serving veterans remains the agency's priority.

With extensive expansion plans and support from the Commonwealth, Veterans Services currently has the opportunity to plan and make certain that they deliver proper benefits and care to veterans, while ensuring that they focus on their clients - Virginia's veterans. However, if management does not take this opportunity to carefully plan their business operations, management and staff may become overwhelmed with delivering services in the newly expanded areas and continue to lose sight of their day-to-day administrative duties.

In the section below, we describe the administrative components of Veterans Services. Specifically, we focus on the agency's administrative duties performed for all service delivery branches and those administrative components for service delivery branches with different processes.

### *Current Administrative Operations*

Currently, Veterans Services has an administrative section that serves the four service delivery branches - benefits, cemeteries, care centers, and veterans' education. This administrative section has a staff of fourteen and provides the following services: payroll, procurement, accounts payable, human resources, information technology, and accounting.

Even though the administrative section is located in Roanoke, adjacent to the Virginia Veterans Care Center (Care Center), it also provides services to the various field offices located throughout the Commonwealth. The administrative section primarily communicates with the other divisions through electronic mail, fax, and regular mail. For example, the benefit offices may either fax or mail payroll timesheets to the central administrative office where the payroll technician processes them.

The service delivery branches also perform processes and communicate these results to the administrative section in different manners. For example, the Care Center processes payroll differently than the other business units and uses an information system application, Kronos, to automate this process by electronically recording times. Care Center employees must scan in and out in order to record their hours worked. The system records these hours and uploads them into the Commonwealth's payroll system. On the other hand, the benefits, cemeteries, and education offices use paper timesheets to record hours worked; these offices submit timesheets to payroll, where the payroll officer manually keys the hours worked into the Commonwealth's payroll system.

The administrative section also does not perform all of the typical administrative duties. Specifically, the Care Center and cemeteries process their own accounts receivable and collect revenues in each individual office. The Care Center currently uses a resident care and billing system, Achieve, to record accounts receivable balances and payments. Once the Care Center has billed and collected funds, Care Center employees submit a summary report to the administrative section for depositing and posting to the accounting system.

The cemeteries simply maintain hardcopy accounts receivable documentation and collect funds from individuals for spousal and eligible dependents' burials. The cemeteries send these funds to the administrative office, where staff deposit the funds and post the total amounts to the accounting system.

### *Planned Future Agency Operations*

With the addition of the new care center, Sitter-Barfoot, Veterans Services' management plans on reorganizing parts of the agency. Management is considering transferring some of the administrative responsibilities to the two long-term veterans care centers, while maintaining a central administrative office that serves the remaining service delivery branches.

The care centers will have payroll, human resources, procurement, accounts payable, and accounting functions and will also retain the accounts receivable function. The central administrative section will continue to perform these responsibilities for the cemeteries, benefits, and veterans' education areas and will submit agency-wide accounting information.

Agency management is currently in the process of hiring a full staff to operate Sitter-Barfoot as a distinct and separate operating unit. Sitter-Barfoot will have two accounts payable technicians, one payroll officer, a procurement officer, three human resource employees, three billing and collections specialists, and a director of finance. These individuals will take on the administrative responsibilities for the facility. Management then anticipates transferring the current Roanoke administrative staff to the Roanoke Care Center.

### *Recommended Future Agency Operations*

Veterans Services has underway some extensive expansion plans for new care centers and cemeteries and as a result management must consider the current and future needs of the agency. The agency must also develop a suitable operating plan and organizational structure to help meet these requirements and ensure that Veterans Services is meeting its mission of serving Virginia's veterans. This plan should detail how the functional areas will support the strategic plan of the organization as well as assess and address the current organization's challenges, including those mentioned later on in this report. Management must also develop a structure that can easily absorb future agency expansions, both planned and unplanned and fully consider opportunities for using technology to perform administrative functions, rather than duplicating operations.

As mentioned later in this report, the administrative section currently receives a lack of detailed, direct, and experienced management guidance and direction. Generally, we found that management oversight, supervisory reviews, and accounting operations are not achieving their internal control objectives and contribute to a number of problems.

As management begins conducting their review of the financial management issues mentioned later, they should consider how this review can help them establish a proper organizational and oversight structure. This review and subsequent actions should help administrative staff receive the direction and guidance they need in order to properly perform their duties and ensure that internal controls are adequate to provide reasonable assurance over the reliability of financial records, effectiveness and efficiency of operations, and compliance with applicable laws, rules, and regulations. Additionally, management should consider the development of operations which minimizes, if not avoids, duplication of function and processes.

If management does not perform this review, then the administrative concerns noted will only compound as the agency expands and adds new offices and staff. The lack of management oversight and guidance may also increase if the agency operates its administrative functions in a more decentralized manner. By having to focus on multiple offices, administrative managers will have to spread limited resources over more offices; as a result, these managers may not have sufficient resources for on-site supervision and monitoring.

In addition, if decentralized operations do not receive adequate management focus, the locations tend to develop their own policies and processes that may not adhere to best practices or have sufficient internal controls. This situation may cause even larger concerns because Veterans Services will have a difficult time ensuring there is an adequate control environment.

While conducting their review and establishing a proper organizational structure, Veterans Services management should consider how administrative functions should interact with the service delivery branches. Administrative functions include human resources, payroll, procurement, accounts payable, accounting, budgeting, and information technology. Management should consider consolidating administrative duties which support the care centers, benefits, cemeteries, and education offices while using technology to prevent

duplication, reduce dependency on having partial systems, and provide both field and agency management with timely and accurate information.

Having both a strong administrative support system and information flow, allows functional management and staff to concentrate on service delivery rather than on back office administrative duties. The proper organizational structure coupled with an appropriate information system will allow the use of administrative resources more wisely by gaining economies of scale, providing sufficient on-site supervision and training, and having adequate segregation of duties.

Organizational structures frequently evolve by consolidating certain processes to improve an entity's performance. Consolidation does not require the physical location of all individuals in the same building; rather, it requires management to assess the environment to determine the most appropriate operating structure, including physical location, organizational hierarchy, and technology for the entire entity. By performing this assessment, management can determine how the entity can best operate as one unit working towards the same goals.

This assessment includes looking at the organization as a whole to take advantage of modern technological processes that can be used throughout the organization, instead of within one individual section. Veterans Services could benefit from this assessment and more fully utilize agency-wide technologies.

For example, the agency currently spends approximately 64 percent (\$13.8 million) of its total operating dollars on personal services and has noticeable turnover in some of their operating areas. The agency could more efficiently and effectively manage its human resources by using an agency-wide human resources management system to track employees, maintain updated personnel information, and record time and attendance. They could avoid maintaining multiple logs and paper forms by entering information directly into the system. In addition, the Veterans Services payroll officer could avoid entering in time for individual employees by requiring all divisions to use an automated time and tracking system. Veterans Services also would only have to input new hire employee information once, instead of multiple times in the agency's payroll system and the Commonwealth personnel management and payroll systems. All offices within the agency could utilize this streamlined, more paperless process to manage human resources.

By consolidating and automating the payroll and human resources process, Veterans Services could combine all payroll responsibilities into one office with one or two payroll officers performing payroll processing duties; this structure would more easily facilitate the necessary on-site supervision and training over the payroll process. Human resources is an essential function of Veterans Services, which requires participation in on-site interviews and trainings; as a result, the agency should maintain a human resources presence at significant offices, such as the veterans care centers, while still having one main office to provide guidance and handle significant or agency-wide issues. This structure would allow individual offices and employees the accessibility they need to perform their duties in a timely manner, but also allow for efficiencies in human resources management.

We have provided just one example of how Veterans Services could assess their organizational structure and technological processes to improve their operating environment. Veterans Services could also implement more modern information systems and processes to reduce duplication of services and unnecessary tasks. By simplifying and eliminating redundant processes, management will have more time to implement much needed improvements in order to meet internal control objectives. This may include additional supervisory reviews, reconciliations, or additional training or documentation.

In addition to reorganizing Veterans Services organizational structure, management must also consider the agency's day-to-day operations. We have noted several concerns in the section below about Veterans Services' internal control environment.



## **INTERNAL CONTROL AND COMPLIANCE FINDINGS AND RECOMMENDATIONS**

Last year, we recommended that Veterans Services establish a more adequate internal control environment, to include:

- developing, implementing, and maintaining management oversight and review,
- documenting policies and procedures and monitoring compliance, and
- ensuring compliance with applicable laws and regulations

While Veterans Services did make changes in some of their processes, this is only an incremental step in establishing an appropriate business and internal control environment. If Veterans Services does not take adequate corrective action, then the concerns noted will continue to become more serious.

During the past year, Veterans Services has hired a number of new individuals to fill positions in the Richmond office. However, the agency still lacks the necessary management to provide the on-site supervision and monitoring necessary to address Veterans Services' internal control environment. Management must take the time to focus on the day-to-day operations of the agency to improve and achieve the basic internal control components. When Veterans Services begins to address the concerns noted below, management must first evaluate the operating environment, then provide sufficient training guidance, and oversight and finally document all policies and procedures to ensure compliance.

### **Evaluate the Operating Environment**

To improve the agency's operations, management must first understand and evaluate their environment to determine what processes are necessary to establish sufficient internal controls. Once management evaluates the environment and decides on the necessary steps to take, they have to establish and implement processes to accomplish the organization's goals. Without assessing the operating environment, management cannot determine what processes are necessary to achieve its goals and may completely miss functions that can improve the organizations' environment. In addition, management could miss establishing operating areas it should address. Detailed below are several issues resulting from a lack of management evaluation of the operating environment.

#### **Reconcile Patient Revenue System to the Commonwealth's Accounting System**

Veterans Services does not have an established process to reconcile the Care Center's internal billing system, Achieve, to the Commonwealth's Accounting and Reporting System (CARS). As a result, Veterans Services has not performed a reconciliation between the two systems.

On a daily basis, the accounting section enters revenue into both systems, but does not ensure that all revenues posted in the billing system equal all patient revenues posted in CARS. Patient revenues totaled \$12.5 million during fiscal year 2007 and accounts for the largest portion of operating revenue for the Care Center, making it essential to reconcile the posted revenue.

By not reconciling the two systems, the Veterans Services cannot ensure that all revenue posted in Achieve is also in CARS. As a result, CARS may not properly state the true revenue of the agency. Veterans Services employees and current management were not aware of the need for this process and how to perform a reconciliation due to the lack of an adequate assessment of patient revenue.

### Properly Perform Reconciliations in a Timely Manner

As noted in the prior audit, Veterans Services does not perform and review reconciliations in a timely manner for petty cash or the resident trust fund accounts, and in some cases, we found that staff could not provide documentation to support that they did a reconciliation. Finally, for the available reconciliations, we found them inconsistently performed and reviewed.

By not performing reconciliations in a timely manner, Veterans Services cannot ensure that it is posting and recording all of the funds and transactions. As a result, management may not detect errors or missing funds.

### Improve Debt Collection Efforts and Account Write-offs

As noted in the prior audit, Veterans Services does not have supporting documentation to show that the Care Center complied with collection procedures for delinquent accounts. In addition, management has not adequately assessed its past-due accounts to determine which accounts should be written-off. Also, Veterans Services does not ensure that staff is properly classifying residents in the appropriate accounts receivable categories.

By not appropriately writing-off accounts, Veterans Services is overstating their accounts receivable by including accounts that are most likely uncollectible. In addition, management is unable to effectively use accounts receivable reports because these reports do not accurately reflect the Care Center's collectible accounts. Without proper classification of accounts, management is unable to properly determine where collections issues are and determine how to address these issues.

Veterans Services should retain supporting documentation for their collection efforts and account classification. Also, management should review the past-due accounts and determine if further collection efforts is worth pursuing or is subject to write-off.

### Establish Adequate Controls over Cemetery Funds

Veterans Services receives a \$300 plot allowance from the federal government for each internment placed in one of the agency's cemeteries. Currently, Veterans Services does not have adequate controls over the reconciliation of these cemetery accounts receivable. Specifically, the agency does not have sufficient policies, procedures, and controls established to ensure that Veterans Services receives all of the federal cemetery internment funds requested. During our review, we found two instances where Veterans Services did not receive the Federal plot allowances after an internment. In addition, Veterans Services does not have adequate controls to ensure the processing and depositing of all cemetery checks in a timely manner.

By not performing reconciliations, the agency can not determine whether it is receiving all of the funds due to the agency. As a result, the agency may not receive all of the Veterans Services' plot allowances.

### Establish a Complete Information Security Plan to Comply with COV Security Policy

As noted in the prior audit, Veterans Services does not have a sufficiently detailed information security program that meets Commonwealth security standards. Some of Veterans Services' operations met the security standard and best practices for information security programs; however, we found issues of noncompliance within the agency's policies. Without a documented information security program, Veterans Services cannot identify or adequately maintain critical information technology components (including data) that the agency relies upon to carry out its business objectives.

Veterans Services needs to establish adequate information security policies and procedures for their data and applications. These policies and procedures help minimize the risk of unauthorized disclosure or alteration of its critical and/or sensitive data. Based on the agency's business objectives, and sensitivity and criticality of data in their ownership, Veterans Services needs to establish, and/or provide more detail for, policies and procedures that include the following components at a minimum:

- Risk Assessment
- Business Impact Analysis
- Business Continuity Plan (also called a Continuity Of Operations Plan)
- Disaster Recovery Plan
- Incident Response Procedure

These components of the information security plan should be applicable to the entire agency and not just the Care Center. The currently developed documents are not available to the entire agency and, therefore, the documents do not uniformly apply to all of Veterans Services.

#### Establish Sufficient System Access Policies and Ensure Appropriate System Access

As noted in the prior audit, Veterans Services does not have sufficient policies governing system access. Current policies do not include processes for adding, modifying, or timely deleting accounts or periodic management review of access.

During our review, we found inappropriate access to Achieve and the Commonwealth's statewide systems. Personnel did not delete one employee's access in a timely manner from the statewide accounting and payroll systems. In addition, several Achieve users have inappropriate administrator access, while others share generic accounts which do not have a specific user associated with the log-on. Veterans Services should grant only administrator access to those accounts which need it to function and assign all accounts to specific users.

Veterans Services also currently uses contract staff to perform access functions for Achieve accounts, including adding and deleting access as requested by the Care Center. This function should be part of the agency since Veterans Services is the data owner and has the proper knowledge to administer data rights.

Policies and procedures for system access are essential to ensure that only appropriate access is given and that user access is deleted when it is no longer necessary to perform an individual's job duties. Users that have inappropriate access or access after their separation date pose a security risk to the organization. Improving access control for the agency will ensure that unauthorized access of data does not occur. Due to the sensitivity of data on the systems at Veterans Services, the agency must have proper controls in place to manage access.

Veterans Services should manage current system access by reviewing and modifying access as necessary to ensure that it is appropriately assigned, including restricting administrator access and assigning all accounts to specific users.

## Comply with the Health Insurance Portability and Accountability Act

Veterans Services does not have sufficient policies and procedures in place to ensure compliance with the Health Insurance Portability and Accountability Act (HIPAA). HIPAA regulations require security in a number of different areas and the federal government mandates that all covered entities abide by HIPAA regulations. Currently, Veterans Services lacks compliance with HIPAA in several sections, including but not limited to, the following:

- Security Management Processes
- Contingency Plans
- Evaluation
- Workstation Security
- Access Control
- Documentation

The requirements for each of these sections exist in the HIPAA Security Rule published by the Federal Department of Health and Human Services. We found Veterans Services is lacking controls that satisfy the requirements for each of these sections. Non-compliance with these HIPAA regulations could lead to civil penalties against the agency.

Veterans Services should review their current HIPAA policies and procedures to determine which areas are non-compliant. Then, management should modify and add those policies and procedures that are not in compliance and communicate the new policies to individuals impacted by HIPAA regulations.

## Appropriately Segregate Information System Service Duties

During our review, we found that Veterans Services does not properly segregate information system services duties. Currently, Veterans Services relies on Virginia Information Technology Agency (VITA) and Northrop Grumman staff to create policies and make policy decisions that should be the responsibility of the agency. The information security officer and/or a security team should drive security policy. When an employee from an external entity drives security policies, Veterans Services' policies may not agree with the agency's business and security requirements.

If Veterans Services' would like to utilize an external entity to create a policy, the agency must create a review and approval process. The review process will ensure that the security policy created matches the agency's direction. Veterans Services' should also provide a copy of the policy created to govern computing requirements to VITA; this will help VITA to perform their duties for Veterans Services.

## Establish Adequate Controls over the Payroll and Human Resources Functions

Veterans Services does not currently have adequate controls over human resources and payroll processes, even though payroll and other personal services account for 64 percent, or almost \$14 million, of the agency's total operating expenses. Specifically, we believe management does not have sufficient policies, procedures, and controls established over a number of payroll and human resources processes. We have concerns about the following areas having a lack of detailed, written policies and procedures:

- Termination processes, including time frames, necessary documentation, and who should be doing what functions,
- Earning, authorizing, and approving overtime and compensatory leave,
- Submission of time cards from field offices from employees instead of supervisors, and
- Distribution of payroll checks, including who distributes them and who may pick up one for another employee

In addition, we have concerns over some of Veterans Services' payroll processes. Currently, Care Center supervisors only return timesheets to the payroll officer if he/she notices a discrepancy. Therefore, as long as no issues arise, supervisors do not indicate approval on timesheets. Veterans Services also does not require employees to indicate the receipt of payroll checks so there is a lack of accountability over the agency's payroll checks.

There is also a lack of segregation of duties over the distribution of payroll checks, reconciliations, and the review of certain payroll reports, since the payroll officer is highly involved in these processes.

During our review, we also found payroll over-payments to employees totaling \$2,582. Veterans Services did not have a complete listing of employees who received payroll over-payments and did not consistently try to recoup these over-payments.

In addition, Veterans Services does not provide sufficient training to its direct supervisors to inform them of their responsibilities for payroll and human resources-related processes. Without this knowledge, supervisors cannot aid Veterans Services in ensuring these processes are functioning as intended.

#### Periodically Review Employee Classifications under the Fair Labor Standards Act

As noted in the prior audit, Veterans Services does not have a sufficient review process for properly classifying employees as exempt or non-exempt under the Fair Labor Standards Act. Even though employees and their job responsibilities change, management does not perform an adequate evaluation to determine whether the position is appropriately classified. By not properly reviewing employee classifications, Veterans Services may not properly classify an employee and as a result, not comply with federal law and Commonwealth policies.

Veterans Services should evaluate employee's classifications on a periodic basis. Management should review the Commonwealth's human resources policies and procedures for guidance. Veterans Services should consult with the Attorney General's office when management is unsure of the appropriate classification.

#### Develop a Plan for Utilizing Federal Veterans Subsidy Funds

Veterans Services receives federal grant subsidy funds for eligible Care Center residents. Federal regulations restrict these funds for financial assistance to States furnishing nursing home and domiciliary care to eligible veterans in State Veterans' homes. During the prior audit, we noted that Veterans Services did not properly classify and report these federal funds.

During fiscal year 2007, Veterans Services did begin to properly classify and report these funds and reported almost \$4.6 million in subsidy funds received; however, the agency still has not established a plan or guidelines for using the grant funds to ensure compliance with federal regulations, even though management spent approximately \$1.3 million during fiscal year 2007. Veterans Services' management did not meet an internally set deadline for developing these policies.

By not developing a plan for using these funds, management cannot ensure that it spends these funds in accordance with federal regulations. In addition, management may not have the opportunity to fully assess the Veterans Services' needs to ensure the most appropriate use of these funds.

### Comply with the Davis-Bacon Act

As noted in the prior audit, Veterans Services does not have adequate internal controls to ensure compliance with the Davis-Bacon Act. Specifically, management lacks a documented process detailing who has the responsibility to verify compliance, how they complete the process, and who will perform the work. As a result, Veterans Services does not verify that the rates paid to the contractor or subcontractors comply with the prevailing wage rates required by the Davis-Bacon Act.

Without established controls and procedures, employees within Veterans Services are unsure who is responsible for compliance and what process to follow in order to comply with the Davis-Bacon Act. By not monitoring the contractors and subcontractors, Veterans Services cannot show that it complied with the Davis-Bacon Act. If Veterans Services does not comply with federal regulations, questioned costs and federal financial penalties may result.

### Establish Adequate Budgets for Individual Cost Centers

Veterans Services does not have an adequate budgeting process that provides division managers with budgets for individual cost centers and categories. In addition, division managers do not receive sufficiently detailed expense and revenue information to allow them to appropriately manage their area and determine how their sections are performing.

Budgeting is a key control and management tool that allows managers to set priorities and goals for the organization. An appropriately set budget with sufficient detail allows managers to set targets and evaluate how individual cost centers are performing. Budgets also allow managers to quickly assess a unit's performance and determine whether there are unusual variances. However, for this process to work properly, management has to develop a detailed budget and periodically compare these amounts to actual revenues and expenses.

### Appropriately Allocate Administrative Costs

As noted in the prior audit, Veterans Services does not appropriately allocate administrative costs to the Care Center and does not have adequate, detailed policies and procedures for allocating these administrative costs. Specifically, Veterans Services charges the entire payroll costs for the accountant to the Care Center even though he performs duties for other areas of the agency. In addition, Veterans Services does not have an adequate process to ensure that current statistics are used to allocate the payroll officer's salary. As a result, Veterans Services is using outdated information to allocate her salary to the Care Center. We also found several arithmetic errors in the administrative cost allocation documentation.

Without a proper allocation method, policy, and process, Veterans Services cannot prevent the inappropriate allocation of costs. As a result, Veterans Services may receive inappropriate reimbursement for indirect costs from Medicaid or other federal grants.

### Implement Appropriate Controls over Inventory

During fiscal year 2007, Veterans Services spent \$1.4 million on food, related supplies, and pharmaceutical drugs. The Care Center does not have adequate controls over this pharmaceutical and food inventory. Currently, staff only take a food inventory for purposes of determining how much to order and a pharmaceutical inventory only to account for the scheduled drugs, as required by federal law. These limited inventory counts do not serve as a tool for management to assess the performance of these sections.

Management does not have a readily available mechanism to determine how much food or pharmaceutical inventory the Care Center has and uses. As a result, management cannot periodically determine whether inventory usage is consistent and reasonable; adequate controls would allow management to identify inventory management problems and recognize inventory misuse or waste.

### Establish Adequate Internal Controls over Fixed Assets

As noted in the prior audit, Veterans Services does not have adequate controls over their fixed assets and does not consistently comply with State regulations. Veterans Services has not established adequate policies and procedures for fixed assets, including when to perform inventories and how to assign a “useful” life to assets. Veterans Services has also not listed a number of fixed assets costing \$5,000 or more, including vehicles, on the Commonwealth’s Fixed Asset Accounting and Control System and has not properly tagged a number of other fixed assets. In addition, Veterans Services does not have adequate documentation to support that it conducted a department-wide inventory during the past two years, as required by Commonwealth regulations.

Without proper recording and tracking of fixed assets, Veterans Services can not maintain and safeguard these items. This increases the risk of misuse and abuse for these assets. Veterans Services should perform a fixed asset inventory at least every two years and properly record and tag their fixed assets.

### Properly Report Construction in Progress

As noted in the prior audit, Veterans Services did not properly report construction in progress for the fiscal year. Specifically, Veterans Services over-reported construction in progress by \$196,296 by improperly including equipment in the reported amount. Prior to fiscal 2007, Veterans Services had not reported construction information as required in Commonwealth financial statement directives. Veterans Services should review construction in progress balances for each capital project and make the necessary corrections to update the fixed asset system to reflect proper information in the future.

### Establish Other Administrative Policies

In our prior report, we noted concerns with Veterans Services’ compliance with the Commonwealth’s procurement, voucher payment, and small purchase charge card policies. In addition, we noted concerns with inconsistent and improper processing of transactions for the Veterans Services Foundation. During our review, we found that the agency has established a better review process to limit the number of individual errors in each of these areas. However, Veterans Services has not established detailed, written policies and procedures over these areas, as it is stated in their corrective action plan.

## **AGENCY OPERATIONS**

Veterans Services has four service delivery branches – benefits, cemeteries, care centers, and veterans' education – and an administrative section. These branches work with the three board-type entities – the Boards of Veterans Services, the Joint Leadership Council of Veterans Service Organizations, and the Veterans Services Foundation – to support the delivery of services to Virginia's veterans.

### **Benefits**

The United States Department of Veterans Affairs provides benefits and services to veterans of the armed forces. These benefits include compensation for service-connected disability or death, income-based pensions, medical care, educational benefits, and home purchase assistance.

The Benefits Service Division assists Virginia's veterans in gaining information and access to the federal benefits and services for which they are eligible. The Benefits Service Division operates a total of 15 field offices across Virginia to provide assistance to eligible veterans. In addition to the field offices, the division also operates 25 itinerant service points to serve veterans. Various government agencies and private entities provide the space for these additional service points. In fiscal year 2007, the United States Department of Veterans Affairs approved 65 percent of the 9,314 claims submitted with help from these offices.

### **Cemeteries**

The Cemeteries Services Division operates two state-owned and operated cemeteries, the Virginia Veterans Cemetery in Amelia and the Albert G. Horton, Jr. Memorial Veterans Cemetery in Suffolk. These cemeteries provide a final resting place for veterans and their eligible dependents.

### **Care Centers**

At the beginning of fiscal year 2004, Veterans Services became responsible for operating the Virginia Veterans Care Center in Roanoke, Virginia. The Care Center provides long-term health care for up to 240 veterans in 120 semi-private rooms. Of the facility's 240 beds, 180 are skilled nursing care beds (including 60 set aside for Alzheimer's patients) and the remaining 60 beds are for assisted-living patients. In fiscal year 2007, the Virginia Veterans Care Center provided 20,056 patient days of assisted living care, out of a capacity of 21,900 patient days – a 91.6 percent occupancy rate. Also in fiscal year 2007, Virginia Veterans Care Center provided 63,407 patient days of skilled nursing, out of a capacity of 65,700 patient days – a 96.6 percent occupancy rate.

Veterans Services substantially completed construction on the Sitter-Barfoot facility in July, 2007. Originally, Veterans Services planned on opening Sitter-Barfoot in early fall, 2007; however, Veterans Services delayed opening the facility primarily because of implementation issues with the patient clinical and billing system (ADL). The delay in implementing the clinical and billing system is due to a lack of technical understanding required to implement ADL in a decentralized environment.

Management currently anticipates opening Sitter-Barfoot in December, 2007. The State Comptroller approved a treasury loan for Veterans Services totaling \$787,100 in September, 2007 to help the facility pay its expenses until it is able to open and generate patient revenue. Veterans Services must repay this loan by December, 2008.



### Veterans Education

In January 2004, Veterans Services assumed the State Approving Agency for Veterans Education function from the Department of Education. This function reviews, evaluates, and approves post-secondary education and training programs offered by educational institutions and various other entities within Virginia. Once the program receives approval, veterans and other eligible individuals may enroll and receive federal financial education assistance. Veterans Services monitors the approved education and training programs to ensure compliance with applicable federal and state regulations.

### Administrative Services

The Administrative Services Division provides the other four service divisions support in the following areas: accounting, budget, human resources, information technology, payroll, and procurement. During fiscal year 2007, Administrative Services implemented a new financial management system which cost the agency approximately \$300,000.

### Veterans Services Foundation

The Veterans Services Foundation serves as an advisory foundation within the executive branch of state government. The Veterans Services Foundation raises funds, identifies existing revenue sources for veterans programs, and administers the Veterans Services Fund. The Department of Veterans Services processes the Foundation's transactions. The foundation spends funds on holiday gifts for the Care Center residents, activities, and other items for the veterans.

## FINANCIAL INFORMATION

Table 1 summarizes Veterans Services' total operating expenses incurred by program area for fiscal years 2006 and 2007. Of the Veterans Services' \$21.8 million in operating expenses for fiscal year 2007, 73 percent is for the Care Center. In fiscal year 2007, personal services accounted for 64 percent of the agency's total operating expenses. Overall, operating expense increased by 13 percent, or \$2.9 million, from fiscal year 2006 to 2007. A large portion of this increase came from personal services due to additional staffing hires in the Care Center and benefit offices and cost-of-living salary increases across the agency.

Table 1

### Operating Expenses by Fiscal Year and Program

<u>Program</u>	<u>2007</u>	<u>2006</u>
Benefits	\$ 2,998,382	\$ 2,560,904
Cemeteries	642,558	505,010
Veterans Education	568,615	40,809
Administrative Services	1,659,224	962,488
Care Center	15,926,047	14,364,006
Veterans Services Foundation	<u>41,448</u>	<u>37,795</u>
Total	<u>\$21,836,274</u>	<u>\$18,971,012</u>

Table 2

### Operating Expenses by Major Category

<u>Category</u>	<u>FY 2007</u>	<u>FY 2006</u>
Personal services	\$13,885,757	\$13,149,366
Contractual services	3,796,357	2,752,217
Supplies and materials	2,420,310	2,268,208
Rent and other continuous charges	1,191,771	751,251
Other	<u>542,079</u>	<u>49,970</u>
Total	<u>\$21,836,274</u>	<u>\$18,971,012</u>

In addition to the operating expenses shown above, Veterans Services also spent over \$22 million on capital projects during fiscal years 2006 and 2007. Veterans Services currently has one large outstanding capital project. During fiscal year 2007, Veterans Services substantially completed construction on Sitter-Barfoot. In addition, during fiscal year 2007, Veterans Services completed general renovations and constructing storage and laundry facilities at the Virginia Veterans Care Center in Roanoke. Veterans Services also spent capital funds on repairing hail damage at the Amelia Cemetery, performing general maintenance, and assessing the need for a new care center in the Hampton Roads area. The table below summarizes the capital expenses for fiscal year 2006 and 2007 for Veterans Services.

Table 3

### Capital Expenses by Fiscal Year and Project

<u>Project</u>	<u>FY 2007</u>	<u>FY 2006</u>
Sitter-Barfoot Veterans Care Center	\$ 11,095,257	\$ 8,687,191
Virginia Veterans Care Center	385,299	1,698,559
Other	<u>8,959</u>	<u>224,318</u>
Total	<u>\$ 11,489,515</u>	<u>\$ 10,610,068</u>

The following table shows the funds available and the total expenses by program for fiscal year 2007. Some programs, such as the Care Center, do not expend all of the program funds available. Central appropriations provided Administrative Services funds available that exceeded actual expenses.

Table 4

Funds Available and Actual Expenses by Program for Fiscal Year 2007

<u>Program</u>	<u>Funds Available*</u>	<u>Actual Expenses**</u>	<u>Difference</u>
Benefits	\$ 3,131,980	\$ 2,998,382	\$ 133,598
Cemeteries	629,632	642,558	(12,926)
Veterans Education	555,802	568,615	(12,813)
Administrative Services	2,048,285	1,659,224	389,060
Care Center	16,547,332	15,926,047	621,285
Veterans Services Foundation	<u>82,050</u>	<u>41,448</u>	<u>40,602</u>
Total	<u>\$ 22,995,081</u>	<u>\$ 21,836,274</u>	<u>\$ 1,158,806</u>

\* Includes Revenue less Refunds, Net Cash Transfers, and General Fund Appropriations

\*\*Includes Expenses less Refunds

Table 5 summarizes Veterans Services' original and final budget to their actual expenses.

Table 5

Budget to Actual Expenses for Fiscal Year 2007

<u>Program</u>	<u>Original Budget</u>	<u>Final Budget</u>	<u>Expenses</u>
Benefits	\$ 3,657,466	\$ 3,213,454	\$ 2,998,382
Cemeteries	682,631	676,395	642,558
Veterans Education	627,859	627,859	568,615
Administrative Services	1,594,755	2,241,834	1,659,224
Care Center	15,626,998	17,051,100	15,926,047
Veterans Services Foundation	<u>-</u>	<u>324,648</u>	<u>41,448</u>
Total	<u>\$ 22,189,709</u>	<u>\$24,135,290</u>	<u>\$21,836,274</u>

The Administrative Services' original fiscal year 2007 operating budget increased by about 29 percent. This increase was primarily the result of an additional increase in the appropriations by the General Assembly and additional funds to support salary and benefit increases.



# Commonwealth of Virginia

**Walter J. Kucharski, Auditor**

**Auditor of Public Accounts  
P.O. Box 1295  
Richmond, Virginia 23218**

November 26, 2007

The Honorable Timothy M. Kaine  
Governor of Virginia  
State Capital  
Richmond, Virginia

The Honorable Thomas K. Norment, Jr.  
Chairman, Joint Legislative Audit  
and Review Commission  
General Assembly Building  
Richmond, Virginia

We have audited the financial records and operations of the **Department of Veterans Services and Veterans Services Foundation** for the period April 1, 2006 through June 30, 2007. We conducted our audit in accordance with Government Auditing Standards, issued by the Comptroller General of the United States.

## Audit Objectives

Our audit's primary objectives were to evaluate the accuracy of recorded financial transactions on the Commonwealth Accounting and Reporting System, review the adequacy of Veterans Services' internal controls, test compliance with applicable laws and regulations, and review corrective actions of audit findings from prior year reports.

## Audit Scope and Methodology

The Department of Veterans Services' management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered materiality and control risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances.

- Federal grant revenues and expenditures
- Expenditures (including payroll)
- Appropriations
- Cash receipting and collections of accounts receivable
- Fixed assets
- Network security

We performed audit tests to determine whether Veterans Services' controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations. Our audit procedures included inquiries of appropriate personnel, inspection of documents, records, and contracts, and observation of the Veterans Services' operations. We tested transactions and performed analytical procedures, including budgetary and trend analyses.

### Conclusions

We found that the Department of Veterans Services properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System. The Department of Veterans Services records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted certain matters involving internal control and its operation and compliance with applicable laws and regulations that require management's attention and corrective action. These matters are described in the section entitled "Internal Control and Compliance Findings and Recommendations."

Veterans Services has not taken adequate corrective action with respect to 14 out of 15 audit findings reported in the prior year. Management took adequate corrective action on the prior year finding entitled "Establish Process for Determining Negotiated Rates."

### Exit Conference and Report Distribution

We discussed this report with management on December 18, 2007. Management's response has been included at the end of this report.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

BEM:clj



**COMMONWEALTH of VIRGINIA**  
*Department of Veterans Services*

Vincent M. Burgess  
Commissioner

Telephone: (804) 786-0286  
Fax: (804) 786-0302

January 4, 2008

Mr. Walter J. Kucharski  
Auditor of Public Accounts  
James Monroe Building, 8<sup>th</sup> Floor  
101 North 14th Street  
Richmond, Virginia 23218

Dear Walt:

Thank you for the opportunity to respond to the 2007 audit findings for the Department of Veterans Services (DVS). The audit was comprehensive and the points and discussions relating to the management structure are consistent with both the short- and long-term goals of the agency. We will continue to take management and administrative actions to resolve deficiencies and to effectively and efficiently manage DVS.

As was noted in the 2007 audit, and as we acknowledged in the exit interview, many items from the 2006 audit were not fully addressed. It is my belief that the plan of correction for the 2006 audit set an overly aggressive timeframe for completing all necessary corrective actions. This aggressive timeframe, coupled with competing priorities and reduced staffing levels, delayed implementation of corrective actions. Examples of the demands placed on the Department in the past year include: implementing a new financial management system, acquiring a new clinical/billing system, preparing to open a new care center, and dealing with the transition to VITA/Northrop Grumman information technology operations. In addition, for six of the last twelve months, the financial and procurement section was short-handed, operating with two fewer staff members than is the norm. The IT position staff member retired and was replaced at mid-year, and DVS currently has only a half-time contracts officer. As a result of these and other challenges, DVS was not fully able to fully implement corrective actions in response to the 2006 audit.

As a part of the 2007 General Fund reduction exercise, DVS gave up funding for three new positions that were to be used to guide and build the structure necessary to correct all previous audit points. While the impact of the loss of these three positions did not have an

impact on the 2007 audit, it does demonstrate that DVS was taking appropriate management action to position itself to operate more efficiently and effectively. As indicated above, delays and restrictions being imposed by the VITA/NG operation have resulted in DVS being one full year behind in the implementation of the financial management system (FMSII). FMSII is only a tool; however, when fully functional, the information provided and the timeframe in which it can be generated, enhances managers' ability to review information and make decisions. In preparing to open the new care center, it was determined that establishing separate agency codes for each facility would enhance the preparation of annual Medicaid/Medicare cost reports and make certification of payrolls more efficient. This action, in fact, tripled the workload for certain processes for the current finance staff, but the workload will be lessened once the new care center is staffed for operations.

While delays have been incurred, actions have been taken to streamline and improve processes. For example, previously it required a minimum of twelve hours to allocate the telephone bill to the appropriate programs and cost centers. Changes made have reduced this processing time to a two-hour maximum. Similar actions have been taken for the allocation of small charge card purchases and for other bills that require allocations to different programs. After several reviews and changes to proposed policies, the Veterans Services Foundation Board of Trustees approved in September 2007 policies and procedures for handling donations made to the care centers and cemeteries. Policies for the small purchasing charge card program were approved and distributed to staff in September 2007, and seven other purchasing/contracting policies have been drafted and are being reviewed, signed off on and distributed as completed. The Department of Accounts performed a Compliance Audit in September 2007, with a focus on travel vouchers, petty cash operations and small purchasing card charge operations, and DVS received a rating of "good" on the report.

Changes in procedures and corrections to deficiencies have been made; however, as indicated, DVS has not tested, audited or established written policies and procedures to document that such changes have occurred. In order to comply with the Agency Risk Management and Internal Control Standards (ARMICS), DVS has been interviewing individuals for a part-time positions that will assist in completion of the ARMICS requirement and at the same time, write policies and standards for operations procedures that will be used to fully address audit points cited in the audit report. It is anticipated that the part-time position will be filled in January 2008, and that it will take six to nine months to complete the necessary work.

A new financial staff position that will focus mainly on the revenue and cost accounting functions of the VVCC is in recruitment and should be filled by the end of January 2008. The duties and responsibilities of this new position will encompass the reconciliation of the patient revenue system, the patient trust fund and the debt collection and account write-offs. A Memorandum of Understanding is being developed with the Department of Rehabilitative Services for assistance in updating and improving existing policies and procedures relating to compliance with Health Insurance Portability and Accountability Act (HIPAA) regulations; and information technology access policies and issues will be addressed at the same time.

Mr. Walter J. Kucharski  
January 4, 2008  
Page 3

Once the part-time internal audit and care center financial positions are filled, new timelines for the completion and implementation of all needed changes and corrections will be developed.

Please let me know if we can provide additional information about our response to any of the audit points, or if you have questions about any of our plans for corrections. I appreciate the efforts of your staff on this audit and particularly your comments and suggestions during the exit conference.

Sincerely yours,



Vincent M. Burgess

cc. The Honorable John W. Marshall  
Secretary of Public Safety

The Honorable Barry R. Green  
Acting Deputy Secretary of Public Safety

Mr. Paul Galanti  
Chairman of the Board of Veterans Services

Mr. J. Armistead Ransone  
Director Finance and Administration

Mr. Colbert L. Boyd  
Chief Operating Officer



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Vince Burgess  
Commissioner

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